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## A Risk Management Agency Fact Sheet

# Selecting a Broker for the Dairy Options Pilot Program

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The Dairy Options Pilot Program (DOPP) is authorized under the Federal Agriculture Improvement and Reform (FAIR) Act of 1996. The U.S. Department of Agriculture (USDA), Risk Management Agency (RMA) is currently expanding this innovative cost-share program in selected States and counties. DOPP helps farmers learn about hedging milk prices through hands-on dairy put options trading. Dairy farmers choose a broker to execute their DOPP transactions from among those registered with the USDA.

## Types of Brokers

One way of classifying brokers is as "discount" or "full-service" brokers. Discount brokers generally just execute the futures or options transactions as instructed by their customers. They may assume that a dairy producer both has a full understanding of the market and can apply the appropriate futures and options strategies.

Full-service brokers, on the other hand, not only execute transactions but also offer other services. They may publish regular market reports, give opinions on where prices are likely to move, and discuss market developments. Because they offer more services, full-service brokers generally charge a higher commission than discount brokers.

So what is the role of commodity brokers? At a minimum, they execute futures and options transactions on an exchange. But they can also establish close relationships with dairy producers that enable those producers to make better decisions and implement sound dairy price risk management strategies. A good broker can play the role of an information provider, a market analyzer, and a consultant.

This fact sheet points out some criteria to consider in selecting a broker for the Dairy Options Pilot Program and is not intended to be comprehensive.

## The Relationship With a Broker

Selecting the right commodity broker is very important. You want a broker whom you trust and in whom you have confidence. Dairy producers should remember that a broker works for them. So you want a broker who is interested in and will take the time to develop a good relationship with you. You have the right to receive the information and advice you need to make quality risk management decisions.

## Criteria To Consider in Selecting a Broker

1. **Location of the broker.** Some people may feel more comfortable working with someone close by. But location may not be the main criterion when it comes to selecting a broker. You want a broker who can serve you well in dairy price risk management. A local broker might not be knowledgeable about the dairy industry. You can develop a good relationship with a knowledgeable broker over the phone.

2. **Knowledge of the dairy industry.** We expect any consultant we use, such as a veterinarian, crop consultant, or nutritionist, to be very knowledgeable about the subject at hand. It could be difficult to obtain good information on dairy price risk management strategies from a broker who knows nothing about dairy farming or milk marketing.

3. **Willingness to manage price risk rather than speculate.** Most brokers are willing to work with producers in helping them implement a sound marketing plan. However, a few brokers might be more interested in recommending speculative positions. Such brokers seek short-term commissions over the long-term interests of dairy producers and should be avoided.

4. **Commissions.** Commissions can be negotiated. The commission you negotiate will depend upon how much you use the services of the broker and your volume of trading. In comparing commissions between brokers, be sure to ask if the commission rate is for a round turn. A round turn commission covers the cost of both entering and exiting a futures or options contract. Some brokers quote round turn commissions and others charge to enter a position and then charge another commission to exit.

5. **Services provided.** You should have a broker explain what services would be provided to you as a customer. For example, a broker might provide daily market information, a weekly market report, a website with information, or other services. You should find out if the broker charges extra for these services or whether they come free of charge. You should also determine if the broker is available at convenient hours to visit with you and to answer your questions.

6. **Resources provided by the National Futures Association (NFA).** You can check on the broker and the brokerage firm by looking on the Internet at the NFA website:

**[www.nfa.futures.org](http://www.nfa.futures.org)** or by calling the NFA Information Center at 1-800-621-3570. By doing so, you can determine if the broker and brokerage firm are in good standing (historical and current). You can view publications that help in understanding the relationship between a producer and a broker. You also have the ability to file a complaint about a broker.

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